■ A SURPRISING 18-MONTH FORECAST: FASTER GROW

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FORTUNE

JANUARY 19, 1987

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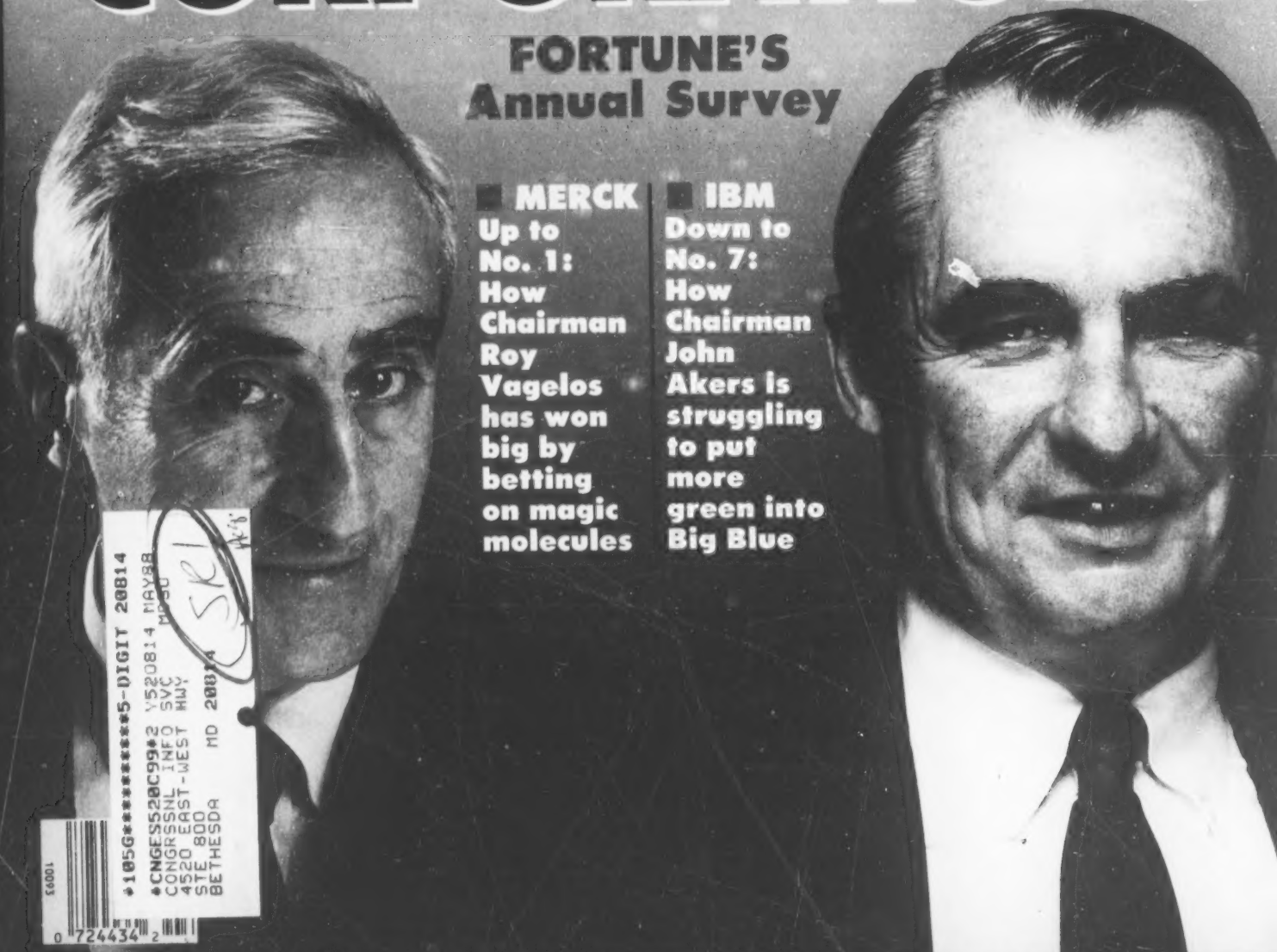
AMERICA'S MOST ADMIRED CORPORATIONS

FORTUNE'S Annual Survey

■ **MERCK**
Up to No. 1: How Chairman Roy Vagelos has won big by betting on magic molecules

■ **IBM**
Down to No. 7: How Chairman John Akers is struggling to put more green into Big Blue



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JANUARY 19, 1987 VOL. 115, NO. 2

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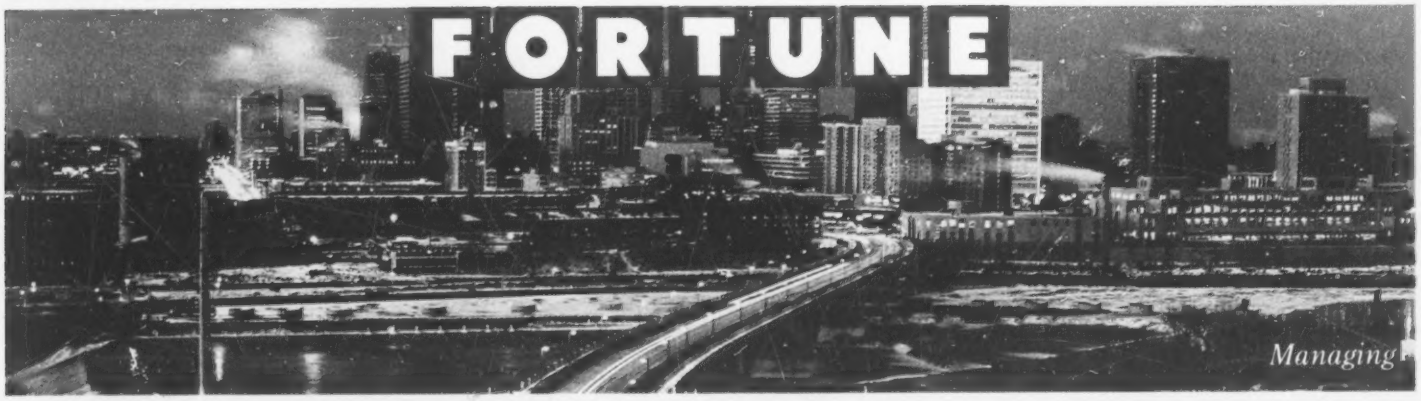

E. J. Camp took this picture of Roy Vagelos (left), the chairman of Merck. IBM's chairman John Akers (right) was photographed by Andy Freeberg. See page 18.

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mailboxes and woos small business people by selling office supplies, printing business cards, and photocopying.

John Bell, former postmaster of Sausalito, California, is an enthusiastic franchisee. He offers a special inducement for students who rent boxes at his San Francisco center. If they phone in, he lets them know if they have received a letter from home, presumably one with a check inside. Who ever heard of calling the U.S. Post Office for such glad tidings?

Capital raises

■ The days of Congressmen crying that they live on peanut butter sandwiches and sleep at the YMCA could soon be over. Federal judges, agency heads, and Congressmen could get hefty raises if the President adopts the recommendations of an independent commission. The betting is that Reagan will be generous, but no softy.

Top federal officials have not had a raise since 1977, while inflation has almost halved the purchasing power of each dollar they earn. "I will likely be required to remortgage my home to educate my son," complains U.S. District Judge Donald Ziegler of Pennsylvania. Small wonder that the government is hard pressed to find and retain good people. Says Ann Banning, Reagan's recruitment director: "It is the wealthy, the very young, and those in the concluding phases of their careers who increasingly constitute our candidate pool."

The federal commission is pushing for pay hikes of up to 80% for some 3,000 officials, at a cost of around $150 million. The souped-up salaries still would not match those of people with equivalent jobs in the private sector. But they would at least transform government service from martyrdom to mere personal sacrifice.

Relief is also at hand for some of the nation's 1.2 million civil servants. Reagan wants to replace seniority raises with merit raises, a switch designed to thrill talented, ambitious bureaucrats, though it may not be so popular with more complacent types. Another proposed change: Government employees would be allowed to make a certain number of heretofore illegal personal calls during working hours.

UNEQUAL PAY ?

GOVERNMENT JOB	PRIVATE SECTOR EQUIVALENT
Secretary of the Treasury Salary now: $86,200 Proposed: $160,000	C.E.O. of major money center bank Average: $585,000
Secretary of Defense Salary now: $86,200 Proposed: $160,000	C.E.O. of major defense contractor Average: $1.2 million
Congressman Salary now: $75,100 Proposed: $160,000	Middle-level partner at top law firm Average: $500,000
Chief Justice of the U.S. Salary now: $108,400 Proposed: $175,000	Chief attorney at large corporation Average: $157,000

SOURCE: BOYDEN INTERNATIONAL

CAPITAL CITIES/ABC, INC.

ABC is refusing to pay stations to air its latest miniseries, Amerika

The coming storm in televisionland

■ Christmas was not very merry for television stations across the U.S. The nation's three major networks, all under frugal new management, are threatening to reduce the millions of dollars they pay affiliates to run their TV shows. The practice, called compensation, dates back to the networks' radio days in the 1920s, when **CBS** and **NBC** adopted it as a way to induce local stations to sign up. In 1986 the networks handed affiliates a staggering $450 million in compensation payments.

The new bosses consider the practice an extravagance. Debate on the subject has been furious. "This is the most complex and emotional issue we have ever dealt with," says Tony C. Malara, senior vice president of distribution for CBS.

ABC threw the first punch in early December, when it told its board of affiliates that it would no longer pay stations to air special events such as the Academy Awards and the Olympics. When the local station chiefs objected, ABC said it would discuss the matter with them again at the end of January. But a week later it transmitted a closed-circuit televised message to the affiliates that it was going ahead with its plan. The first uncompensated broadcast: *Amerika*, a controversial miniseries about life in the 1990s following a Soviet takeover of the United States, set to run beginning February 15.

CBS may phase out compensation for stations in the top 100 markets—from Lansing, Michigan, on up to New York—over three years. The rationale: Large stations depend on compensation much less than small ones. NBC, the top-ranked network, says it has no immediate plans to cut compensation; industry executives say it is merely waiting to see what the competition does.

To the affiliates, the networks' plans are ill conceived. "The networks are doing the right thing in trying to cut costs; they've just found the wrong

AMERICA'S MOST ADMIRED CORPORATIONS

The king is dethroned: IBM, No. 1 since the survey began, drops to seventh place. Long live the king: Merck is the new leader among 300 big companies. GM plunges from No. 16 to No. 109. Bringing up the rear are LTV and—no surprise—BankAmerica. ■ *by Edward C. Baig*

IN ALL the first four years of FORTUNE's annual survey of the most admired companies in America, one corporation has reigned as No. 1. But not in the latest survey. IBM is still right up there among the top ten of 300 American companies rated by thousands of corporate officers and other experts, but it has fallen to seventh place. Big Blue is blushing a bit. "I'd much rather be first," says John Akers, IBM's chief executive. "We've gone from being perhaps too invincible to perhaps having more problems than people expected."

The new king: Merck, the New Jersey–based pharmaceutical company. Merck, fifth overall a year ago, has made news with some of the hottest new drugs on the market—including Vasotec for high blood pressure and Primaxin, an injectable antibiotic for severe bacterial infections. (For an appraisal of the strategy and future of IBM and Merck, see the following articles.)

Merck and IBM are the only companies that have appeared in the top ten in all five annual surveys. Boeing, the new No. 3, and Dow Jones, No. 9, have made the cut four straight years. Other top ten repeaters: Rubbermaid (No. 5) and J.P. Morgan (No. 4). Three companies make their first appearance at the top: Liz Claiborne, at No. 2; Shell Oil, No. 6; and Herman Miller, No. 10.

Competition among the elite is heating up. Exxon was squeezed out of the ten best despite a slight increase in its approval score. The oil giant is 13th, just above Coca-Cola, another dropout from last year's top ten. 3M, last year's runner-up, finds itself in 19th place this time; Procter & Gamble, No. 8 a year ago, slipped to No. 16.

The ten most admired companies have made lots of money for their stockholders. Their median return on equity for 1985 was 19.75%, and every one bested the FORTUNE 500's median ROE of 11.6%. The most admired list's 1985 median total return to investors—stock price appreciation plus dividends—was an outstanding 49.9%, vs. 26.3% for the 500. Total return for the longer term isn't bad: The median for the top ten was 18.8% annually over ten years, against the 500's 17.04%. By contrast, total return for the ten companies on the least admired roster was dismal—a median of just 2.7%.

That least admired list is littered with money losers and repeaters. Seven of the bottom ten were in the red in 1985; eight out of ten have been among the bottom group at least once before. And two—American Motors and Pan Am—are the antitheses of IBM and Merck: They have been among the ten least admired companies in all five surveys. Asbestos-plagued Manville is a four-time loser; Financial Corp., a savings and loan giant, has been in the bottom ten three times.

LTV, BankAmerica, and Bethlehem Steel were among the least admired a year ago. And Trans World Airlines, a cellar dweller twice before, is back after a one-year absence from the survey, which is limited to the top ten companies in sales or assets for each industry. Manhattan Industries, new to the survey, and Union Carbide, new to the bottom ten, round out the list of losers. Two of last year's ten bottom fish barely escaped this time: Amax and Control Data floated up to 12th and 11th from the survey floor.

FORTUNE's corporate reputations survey ranks the ten largest companies in each of 33 industry groups that appear in the annual FORTUNE 500 and FORTUNE Service 500 directories of industrial and nonindustrial corporations. (In groups that have fewer than ten companies, fewer than ten are ranked.) The groups are based on categories estab-

REPORTER ASSOCIATE *Barbara Hetzer*

HOW IT WAS DONE

■ To compile the rankings of 300 companies in 33 industry groups, FORTUNE late last year polled more than 8,200 senior executives, outside directors, and financial analysts. About half responded—a good return. One who declined was Lee Iacocca. "I am afraid my bias might skew the results of your study," wrote the Chrysler chairman. (Even without his vote, however, Chrysler finished a strong second behind Ford in the motor vehicles group.) Respondents were asked to rate the companies in their own industry on eight key measures of reputation, using a scale of 0 (poor) to 10 (excellent). The eight attributes are: quality of management; quality of products or services; innovativeness; long-term investment value; financial soundness; ability to attract, develop, and keep talented people; community and environmental responsibility; and use of corporate assets.

ILLUSTRATIONS BY SHELLEY DANIELS. PHOTOGRAPHED BY GALANTE MARZELLI

AT THE TOP AND BOTTOM OF THE 300 COMPANIES

RANK	COMPANY	SCORE
1	**Merck** Pharmaceuticals	8.38
2	**Liz Claiborne** Apparel	8.02
3	**Boeing** Aerospace	7.99
4	**J.P. Morgan** Commercial banking	7.95
5	**Rubbermaid** Rubber and plastic products	7.94
6	**Shell Oil** Petroleum refining	7.91[1]
7	**IBM** Office equipment, computers	7.91[1]
8	**Johnson & Johnson** Pharmaceuticals	7.86
9	**Dow Jones** Publishing, printing	7.84[2]
10	**Herman Miller** Furniture	7.84[2]

The most admired

Merck dethrones IBM, No. 1 since the survey began and the only other company in the top ten every year. Liz Claiborne and Herman Miller make their debut.

RANK	COMPANY	SCORE
300	**LTV** Metals	3.11
299	**BankAmerica** Commercial banking	3.28
298	**American Motors** Motor vehicles and parts	3.45
297	**Financial Corp. of Amer.** Savings institutions	3.46
296	**Manville** Glass, building materials	3.64
295	**Bethlehem Steel** Metals	3.69
294	**Pan Am** Transportation	3.73
293	**Union Carbide** Chemicals	4.16
292	**Manhattan Industries** Apparel	4.30
291	**Trans World Airlines** Transportation	4.31

The least admired

LTV and Manville are both in Chapter 11 and back at the bottom of the list. The least admired company of 1985, Financial Corp. of America, moves up a little.

[1]Shell Oil scores higher than IBM in five of eight attributes.
[2]Dow Jones scores higher than Herman Miller in six of eight attributes.

lished by the U.S. Office of Management and Budget. To appear in the survey, an industry group must contain at least four companies.

The latest study, which evaluates 300 companies, adds two categories to the previous list—furniture, which contained only three companies last year, and savings institutions, a split-off from the diversified financial classification. Companies are assigned to industry groups according to the business that contributed most to 1985 sales. Some umpiring is required. For example, since Trinova Corp. (formerly Libbey-Owens-Ford) did not sell off its glass business until April 1986, it is rated among building material companies rather than among industrial and farm equipment concerns, where it believes it belongs. Because Household International disposed of all its retailing operations before the start of 1986, it was eliminated from the survey.

OF THE TEN companies whose average point scores (see box) changed the most, only four improved. H.F. Ahmanson and Great Western Financial, both Southern California savings and loans, made the largest leaps. Largely because its profits quadrupled in 1985, Ahmanson jumped 173 places to No. 47 overall; Great Western, whose profits doubled that year, hurdled 176 places to No. 34. Increased mortgage lending, stimulated by lower interest rates, helped both S&Ls rebound from the money-losing years of the early 1980s. The two S&Ls finished first and second in the new savings institution category. A year ago, as diversified financial companies, Great Western and Ahmanson were seventh and eighth respectively.

Toymakers and vehicle manufacturers dominate the list of companies that lost the largest number of points. Hurt by a decline in popularity of some of their biggest sellers were Mattel, which makes the Masters of the Universe line, and Coleco, producer of Cabbage Patch Kids. Mack Trucks and Fruehauf skidded off the highway; GM went over a cliff, plummeting from 16th place to 109th. GM profits have sagged, Saturn small-car production has been delayed, and the company has announced that it will close nine plants and parts of two others employing some 29,000 workers in all. GM dropped in all eight attributes of reputation rated by FORTUNE's experts, with quality of management sinking from No. 13 a year ago to No. 153. Says David Healy, an auto analyst with Drexel Burnham Lambert: "I suppose three years ago Chief Executive Roger Smith was a hero. Today Roger Smith is a bum."

Quality of management

MOST ADMIRED	SCORE
Liz Claiborne	8.98
J.P. Morgan	8.53
Rubbermaid	8.49

LEAST ADMIRED	SCORE
BankAmerica	3.15
LTV	3.33
Pan Am	3.96

Quality of products or services

MOST ADMIRED	SCORE
Dow Jones	8.77
Merck	8.75
Boeing	8.73

LEAST ADMIRED	SCORE
American Motors	4.33
Financial Corp. of America	4.31
Pan Am	4.69

The new champion, Merck, finished first handily. It beat runner-up Liz Claiborne by 8.38 points to 8.02. Merck ranked first overall in long-term investment value and ability to attract, develop, and keep people, and finished no lower than fifth in any other attribute. "Because we're in the business of improving people's health," says P. Roy Vagelos, the M.D. who runs Merck, "our reputation is probably more important than the amount of money we make." Vasotec and Primaxin brought in around $300 million of Merck's estimated $4 billion in 1986 sales. Within its industry, Merck finished first in seven attributes and was second only to Johnson & Johnson in community and environmental responsibility.

Liz Claiborne Inc., which has helped many professional women achieve a stylish look, has tailored a nifty corporate image for itself. One of the youngest companies ever to make the FORTUNE 500—it got on that list after just ten years—Liz Claiborne is first in innovation and in quality of management, though you'd have a hard time convincing President Liz Claiborne of it. "We keep criticizing ourselves for how poorly we manage the company," says the boss, whose name is sewn on every label. Claiborne's management, which takes a team approach, appears to be cut from finer cloth than that of most other firms in the rag trade, a notoriously mismanaged bunch. So does its stock performance. The share price has multiplied 29 times since the company went public in 1981.

Climbing three notches to No. 3 overall, Boeing ranks third among all companies in both quality of products and services and ability to attract people, and fourth in quality of management. Boeing outfinanced its nine aerospace competitors in every attribute of reputation. In 1986 the company wrote some 340 new airplane orders worth about $29 billion, helped by the 747-400, a lighter, more efficient version of its popular jumbo jet that will go into service in 1988.

J.P. Morgan has deposited itself in fourth place, up from tenth a year ago. The conser-

Innovativeness

MOST ADMIRED	SCORE
Liz Claiborne	9.00
Comsat	8.41
Herman Miller	8.37

LEAST ADMIRED	SCORE
Bethlehem Steel	3.29
BankAmerica	3.31
American Motors	3.75

Financial soundness

MOST ADMIRED	SCORE
Exxon	9.25
IBM	9.14
Merck	8.98

LEAST ADMIRED	SCORE
LTV	1.38
BankAmerica	1.81
Financial Corp. of America and American Motors (tie)	1.89

Community and environmental responsibility

MOST ADMIRED	SCORE
Johnson & Johnson	8.21
IBM	7.93
Merck	7.69

LEAST ADMIRED	SCORE
Manville	5.67
LTV	5.74
A.H. Robins	5.88

Long-term investment value

MOST ADMIRED	SCORE
Merck	8.67
R.J.R. Nabisco	8.43
Philip Morris	8.31

LEAST ADMIRED	SCORE
LTV	1.90
American Motors	3.39
Bethlehem Steel	3.50

Ability to attract, develop, and keep talented people

MOST ADMIRED	SCORE
Merck	8.50
J.P. Morgan	8.33
Boeing	8.33

LEAST ADMIRED	SCORE
BankAmerica	3.59
LTV	3.60
American Motors	3.93

Use of corporate assets

MOST ADMIRED	SCORE
R.J.R. Nabisco	8.11
Merck	8.08
Liz Claiborne	8.08

LEAST ADMIRED	SCORE
BankAmerica and LTV (tie)	3.65
Financial Corp. of America	3.93

native commercial bank is second in both quality of management and ability to attract, develop, and keep talented people. It ranks fourth in nine use of corporate assets, and fifth in both value as a long-term investment and soundness of financial position. Through the third quarter of 1986, Morgan outperformed all major banks in return on assets, return on equity, and loan quality. For Chairman Lewis Preston, keeping good people around may be the hardest of the attributes to maintain. "Tigers move faster than old tigers," he says. Preston says, "We generally lose people to investment banks or to industry. If we lose to other banks, the fellow who moves ought to have his head examined."

No. 3 Rubbermaid's success is based on a constant stream of new products—more than 300 over the past five years, from microwave cookware to plastic patio furniture. No. 7 overall a year ago, Rubbermaid ranks third in quality of management, fifth in quality of products and services, and in the top ten for three other attributes. The company is meeting most of the goals Chairman Stanley Gault set in 1980: net income and earnings per share have grown on a compounded annual basis by at least 15%; sales growth falls just short at 14.5%.

The sixth-place ranking of Shell Oil may reflect some confidence in its parent, the Royal Dutch/Shell Group of the Netherlands and Britain. Shell Oil, which operates independently, saw earnings decline more than a third during the first nine months of 1986. Despite the profitability problems affecting its industry, Shell ranks fourth in financial soundness, fifth in use of corporate assets, and seventh in management quality, innovativeness, and ability to attract, develop, and keep good people. "You have to be willing to challenge people and always advance them a little bit sooner than you think you should," says John Bookout, Shell's chief executive. The downside of that approach: "We did the holes with people just like we did the holes looking for oil and gas." Within its industry, Shell is tops in all but three categories; rival Exxon wins out for financial soundness, value as a long-term investment, and corporate responsibility to the environment.

AT IBM, the chips are down. "The short-term financial performance of the company isn't up to our expectations, the investing public's expectations, or our customers' expectations," says C.E.O. Akers. "I would expect that in the current climate [since, we will be back]. Among all 300 companies that cost IBM ranks second in financial soundness, fifth in ability to attract people, eighth in long-term investment value, ninth in quality of management, and ninth in use of corporate assets. Last year it was first in all three attributes. IBM improved in one ranking, climbing from No. 4 to No. 3, in environmental and community responsibility. The company shares several scores of that responsibility to November. In that time IBM announced that to increase operating efficiency it would close down a major parts-distribution center in

Greencastle, Indiana. But IBM said it would lay off no employees. Instead, everyone will be offered new jobs elsewhere. IBM has proposed to give the community the 234-acre site and the 350,000-square-foot building.

"The place reputation really counts is with your customers," says James Burke, chairman of Johnson & Johnson. Eighth overall, up from 11th last year, the company ranks first in responsibility to community and environment. "We got a lot of visibility due to the Tylenol crisis," says Burke. No. 9 Dow Jones, publisher of the *Wall Street Journal* and *Barron's*, ranks highest for quality of products and services for the fourth year in a row. But sluggish national advertising at the *Journal* and other publications may account for Dow Jones's slip from third place overall last year. The company dropped from No. 3 to No. 10 in soundness of financial position, and from No. 3 to No. 11 in value as a long-term investment.

Newcomer Herman Miller, the manufacturer of office furniture, rounds out the top ten. Of the ten most admired companies, the Zeeland, Michigan, firm has the highest total return on an annual basis: 49.75%. Earnings have grown an average of 30% a year for a decade. No. 3 for innovation, Herman Miller showed its stuff in September by introducing a "silver parachute plan" under which workers with at least two years' service are entitled to a full year's severance pay in the event of a hostile takeover.

EMPLOYEES OF the companies at the bottom of the pile should be so lucky. LTV, least admired of the 300 companies, is barely breathing. Toiling through Chapter 11 proceedings, the stumbling steelmaker, second largest in the U.S. after USX, scored a rusty 3.11. LTV wrote off $2.1 billion in the third quarter, which could have the effect of shifting some of its pension obligations to the federal Pension Benefit Guaranty Corp. The quarterly charge against earnings was the second largest in U.S. corporate history; AT&T took a $5.5-billion hit in 1983, just before its breakup. LTV stands no higher than 294th in any attribute (quality of products or services) and comes in last, at a piddling 1.38, for value as a long-term investment and soundness of financial position. Within the metals group, LTV is the worst performer in every category except innovativeness, where Bethlehem Steel ranks last.

Additional write-offs or bankruptcies could happen at other metals companies. A possible candidate: Bethlehem, No. 295 on the survey and next to worst in the seven attributes besides innovation. The company lost $187 million through the first nine months of 1986, and Chairman Walter Williams has set no timetable for renewed profitability. "There are too darn many uncertainties ahead," he says. Since 1982 Bethlehem has shed over 30% of its raw steel-making capacity, dropping to less than 16 million tons, and further cutbacks are likely. It has paid no dividends on its common stock since 1985, and last year it sold off an engineering subsidiary and several other operations not involved with making steel.

BankAmerica deposed C.E.O. Samuel Armacost and brought back an old warrior to try to reverse the corporate fortunes. More

THE MIXED FATE OF THE CLASS OF 1983

■ How have the fortunes of the companies at the top and bottom of the initial FORTUNE corporate reputation survey changed since the first lists were published in January 1983? Would the stocks of those most admired companies have been a better investment than the stocks of the least admired? Answers: Most of the top ten in the original survey of 200 companies still get high marks from their peers—and from investors. Less expectably, the stocks of some of 1983's lowest-ranking ten have been plum pickings for contrarians. (Total returns were calculated using stock prices at the end of 1982 and at the end of November 1986, or earlier in case of a takeover. The results assume that dividends were reinvested at the end of each calendar year.)

Only three of 1983's least admired ten appear in the current survey. RCA, No. 194 of the 200 companies in the original survey, was acquired last June by No. 9, General Electric; from year-end 1982 through the time of the merger, RCA's annualized total return to its shareholders was 40%, second best of all 20 companies top and bottom. Crown Zellerbach investors earned a decent 20% a year until James River Corp. of Virginia (No. 94 on this year's list) bought the company in October. And assuming they grabbed the money and ran, investors earned a nifty 31% annualized return when Republic Steel was taken over in June 1984 by LTV, the least admired company today. A&P and Woolworth, too small to qualify for the current survey, made bargain hunters happy. Boosted by improved margins, the stocks of both retailers outperformed all top ten companies in 1983's survey.

Some corporate wallflowers failed to blossom. International Harvester, now Navistar International, and National Steel, absorbed into National Intergroup, have fresh names if not fresh prospects. Navistar crawled out of the bottom ten—barely—and earned a mediocre return. In the continuing steel slump, the stock of National Intergroup hit the pits. So did Tesoro Petroleum, an oil field services company hurt by lackluster drilling activity, and American Motors, stuck in the mud since 1983.

1983: The most admired companies

1983 RANK	THIS YEAR	COMPANY	TOTAL RETURN
1	7	IBM	10.83
2	23	Hewlett-Packard	5.13
3	8	Johnson & Johnson	11.32
4	70	Eastman Kodak	9.32
5	1	Merck	29.62
6	106	AT&T	21.36
7	15	Digital Equipment	20.68
8	135	SmithKline Beckman	12.08
9	22	General Electric	19.01
10	47	General Mills	25.10

. . . and the least admired

1983 RANK	THIS YEAR	COMPANY	TOTAL RETURN
200	284	International Harvester[1]	7.42
199	—	A&P	32.23
198	298	American Motors	(17.46)
197	294	Pan Am	11.87
196	—	F.W. Woolworth	41.83
195	—	Crown Zellerbach	19.66[3]
194	—	RCA	40.16[4]
193	—	Republic Steel	30.60[5]
192	—	Tesoro Petroleum	(7.21)
191	—	National Steel[2]	(2.42)

[1]Name changed to Navistar International, February 21, 1986.
[2]Name changed to National Intergroup, as part of restructuring, September 13, 1983.
[3]Through October 30, 1986, acquired by James River Corp. of Virginia.
[4]Through June 9, 1986, acquired by General Electric.
[5]Through June 29, 1984, acquired by LTV.

than five years after he left to head the World Bank, A.W. Clausen, 63, took the helm again in October. He has his work cut out for him. BankAmerica ranked No. 299 overall and last among commercial banks in every key attribute except community and environmental responsibility, where it came in No. 8. Through the first three quarters of 1986, BankAmerica lost $600 million and accumulated loan losses of $1.5 billion. Its loan quality was the worst among all major banks, with a 4.4% ratio of nonperforming assets to total assets (J.P. Morgan's was 0.89%). First Interstate, a bank half BankAmerica's size, is making a takeover run at the company.

American Motors is parked in a familiar spot. At No. 298, the money-losing automaker is near the bottom again. Although its Jeep models have consistently won industrywide awards for best four-wheel-drive vehicles, AMC gets the worst mark of all companies for quality of products and services. The company expects a profit for the last quarter of 1986, and it's betting the garage on a new line of bigger Renault models produced at a $675-million plant in Canada.

FINANCIAL Corp. of America escaped the cellar, but not by much. The largest U.S. savings institution, which owns American Savings & Loan Association, it is in the 297th position this time. In its category, FCA ranks tenth in every attribute. Although one of only three least admired companies to show a net profit in 1985, FCA is still losing money on an operating basis. The problem: delinquent loans. Chairman William Popejoy is putting on his best face. He expects a "meaningful" operating profit in the fourth quarter. And the best news, he says, is that just two years after FCA lost $590 million, the biggest ever for an S&L, "people don't talk about us failing anymore."

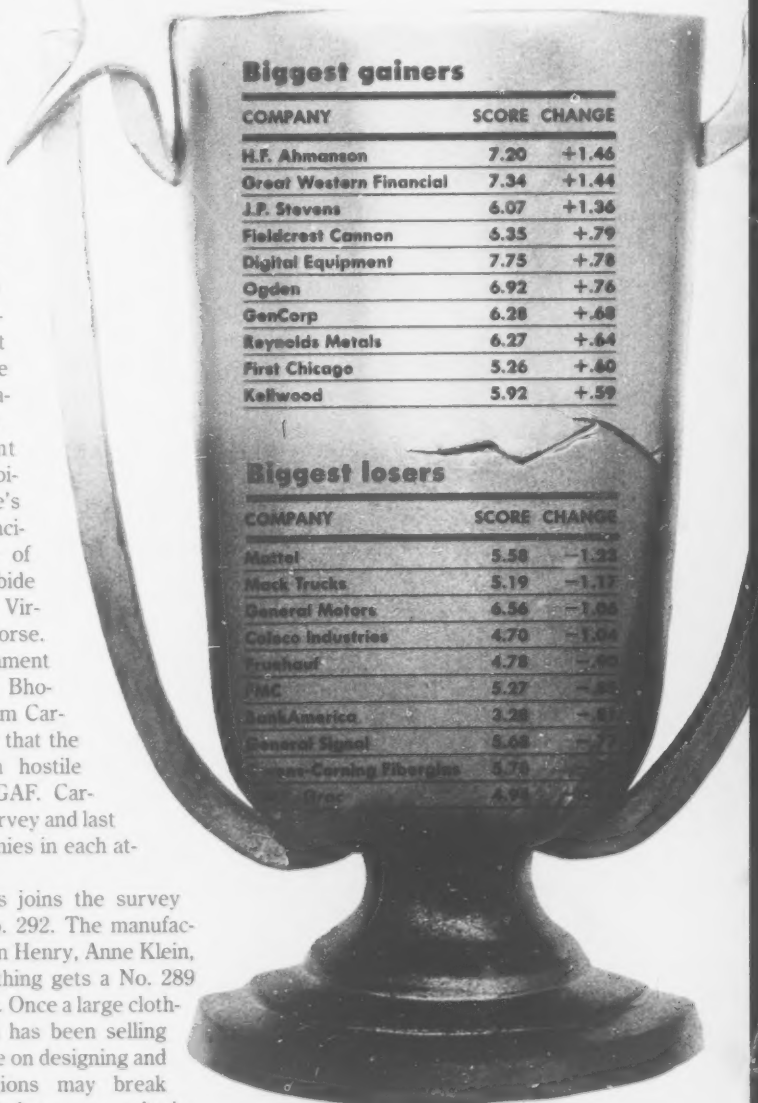
Though No. 296, Manville Corp., uses golfing great Jack Nicklaus as a spokesman in television commercials, the company is still a long way from the green despite its new management. Manville has been in Chapter 11 since August 1982, but it might finally escape in 1987. A reorganization plan that included a $2.5-billion to $3-billion trust fund for asbestos victims was approved in December by all of the company's creditors except common shareholders. (Two groups of shareholders are attacking the plan in the appeals courts.) Manville ranks last in community and environmental responsibility. "I think that perception is increasingly less deserved," says Barbara Alexander, a Salomon Brothers analyst. "But I wouldn't expect it to change until the company is operating out of the constraints of bankruptcy."

Trans World Airlines, No. 291, and Pan Am, No. 294, can't get their reputations to take off. Within the transportation industry, they fare no better than ninth in any attribute. Terrorism killed traffic on transatlantic flights, stinging Pan Am especially hard, since it sold off its Pacific routes to United in 1985. Clearer skies may be ahead. Pan Am is aggressively challenging Eastern with hourly shuttle flights between New York and Boston and Washington. TWA made what analysts think is a smart pickup in Ozark Air Lines. Under Carl Icahn, TWA is paring down. "He's probably saved the company $600 million to $800 million a year on the cost side," says Candace Browning, an airline analyst at Wertheim & Co.

The Bhopal accident late in 1984 began the poisoning of Union Carbide's reputation, and a later incident involving release of toxic gases at a Carbide plant in Institute, West Virginia, made matters worse. Then the Indian government rejected a $350-million Bhopal settlement offer from Carbide, and not long after that the company fought off a hostile takeover attempt by GAF. Carbide is No. 293 in the survey and last among chemical companies in each attribute of reputation.

Manhattan Industries joins the survey near the bottom, at No. 292. The manufacturer of Perry Ellis, John Henry, Anne Klein, and other designer clothing gets a No. 289 rating in product quality. Once a large clothing retailer, Manhattan has been selling off stores to concentrate on designing and manufacturing. Operations may break even for the year, partly because results include $5 million from insurance following the death of designer Ellis.

Old perceptions, good and bad, may be hard to change, but as IBM and others have discovered, the mold is breakable. Reputations are built on first-class management, along with high-quality products and services —the two attributes that respondents consistently consider the strongest components of a corporate image. But companies are only as strong as their latest balance sheets. Once they slip, how easy is it to climb back up the reputation ladder? "Glass, china, and reputation, are easily crack'd and never well mended," Benjamin Franklin said. The LTVs and Manvilles of corporate America would like to prove him wrong.



Biggest gainers

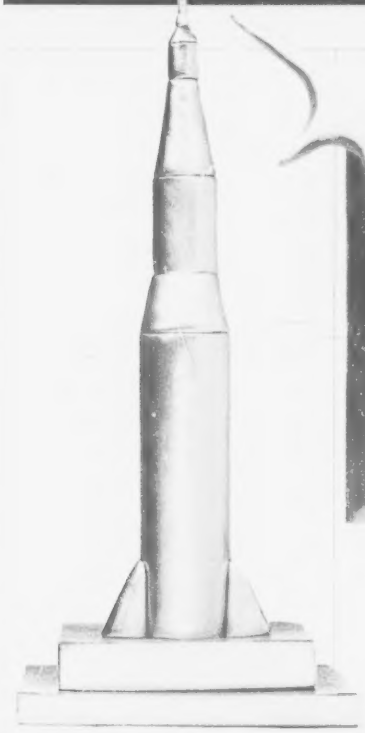
COMPANY	SCORE	CHANGE
H.F. Ahmanson	7.20	+1.46
Great Western Financial	7.34	+1.44
J.P. Stevens	6.07	+1.36
Fieldcrest Cannon	6.35	+.79
Digital Equipment	7.75	+.78
Ogden	6.92	+.76
GenCorp	6.28	+.68
Reynolds Metals	6.27	+.64
First Chicago	5.26	+.60
Kellwood	5.92	+.59

Biggest losers

COMPANY	SCORE	CHANGE
Mattel	5.58	−1.32
Mack Trucks	5.19	−1.17
General Motors	6.56	−1.05
Colgate Industries	4.70	−1.04
Pruehauf	4.78	−.90
FMC	5.27	−.83
BankAmerica	3.28	−.81
General Signal	5.68	−.77
Owens-Corning Fiberglas	5.70	−.73
Grace	4.99	−.72

Changes in Score

Higher profits helped boost H.F. Ahmanson and Great Western Financial, both California S&Ls, by nearly a point and a half. Biggest loser Mattel hasn't had a hit new toy in a while.



HOW COMPANIES RANK IN 33 INDUSTRIES

Industry groups are based on U.S. Office of Management and Budget categories. Companies are assigned to industries according to the business that contributed most to 1985 sales.

Aerospace

Boeing leads in every attribute, but Martin Marietta rocketed up three places after a restructuring.

RANK	LAST YEAR	COMPANY	SCORE
1	1	Boeing	7.99
2	5	Martin Marietta	7.07
3	2	Rockwell International	6.87
4	3	Lockheed	6.76
5	7[1]	Northrop	6.75
6	4	McDonnell Douglas	6.69
7	7[1]	United Technologies	6.38
8	9	General Dynamics	6.29
9	10	Textron	6.03
10	–	Allied-Signal[2]	5.92

Beverages

Coca-Cola rates spritziest in product quality, financial soundness, investment value, and two other categories.

RANK	LAST YEAR	COMPANY	SCORE
1	1	Coca-Cola	7.80
2	3	PepsiCo[4]	7.52
3	2	Anheuser-Busch	7.50
4	4	General Cinema	6.32
5	7	Joseph E. Seagram & Sons	6.03
6	9	Adolph Coors	5.91
7	6	Brown-Forman	5.75
8	8	G. Heileman Brewing	5.49

Apparel

Liz Claiborne and Manhattan Industries join the list for the first time. Claiborne is No. 2 overall.

RANK	LAST YEAR	COMPANY	SCORE
1	–	Liz Claiborne[3]	8.02
2	1	VF	7.50
3	2	Hartmarx	6.72
4	3	Interco	6.31
5	9	Kellwood	5.92
6	5	Oxford Industries	5.89
7	8	Phillips-Van Heusen	5.69
8	–	Manhattan Industries[3]	4.30

[1]Tie. Each scored higher than the other last year on four of eight attributes.
[2]Ranked No. 3 last year in the chemicals category. Acquired Signal Cos., ranked No. 6 last year in the aerospace category.
[3]Not ranked last year.
[4]Acquired MEI Corp., ranked No. 5 last year in the beverages category.

Chemicals

Dow is No. 1 in management quality and use of corporate assets, but Du Pont is tops in the other six attributes.

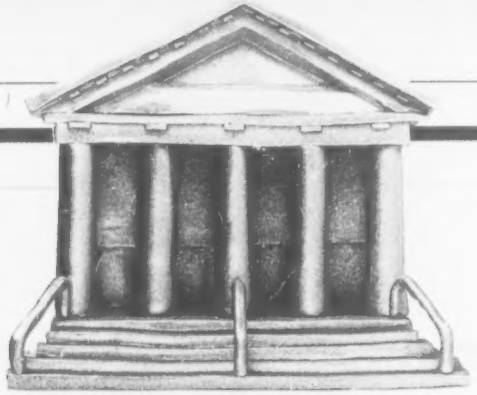
RANK	LAST YEAR	COMPANY	SCORE
1	1	Du Pont	7.41
2	2	Dow Chemical	6.93
3	5	Monsanto	6.40
4	4	Hercules	6.26
5	7	Celanese	6.20
6	6	American Cyanamid	6.17
7	–	BASF[1]	6.05
8	8	FMC	5.27
9	9	W.R. Grace	4.94
10	10	Union Carbide	4.16

Diversified financial

American Express is No. 1 or No. 2 in every category; E.F. Hutton, bruised by legal problems, ranks last in seven.

RANK	LAST YEAR	COMPANY	SCORE
1	2	American Express	7.27
2	1	First Boston	7.15
3	–	Loews[1]	6.50
4	–	Bear Stearns[1]	6.36
5	3	Merrill Lynch	6.33
6	5	Aetna Life & Casualty	6.18
7	4	Travelers Corp.	6.04
8	9	Federal National Mortgage Assn.	5.64
9	6	Cigna	5.42
10	–	E.F. Hutton[1]	4.81

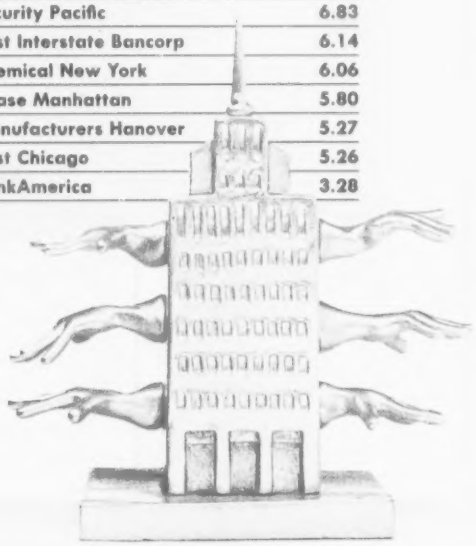
[1]Not ranked last year.
[2]Formerly Phibro-Salomon.



Commercial banking

J.P. Morgan leads in six categories; BankAmerica is No. 10 except in responsibility, where it's eighth.

RANK	LAST YEAR	COMPANY	SCORE
1	1	J.P. Morgan	7.95
2	2	Citicorp	7.26
3	3	Bankers Trust New York	7.05
4	4	Security Pacific	6.83
5	5	First Interstate Bancorp	6.14
6	6	Chemical New York	6.06
7	7	Chase Manhattan	5.80
8	8	Manufacturers Hanover	5.27
9	9	First Chicago	5.26
10	10	BankAmerica	3.28

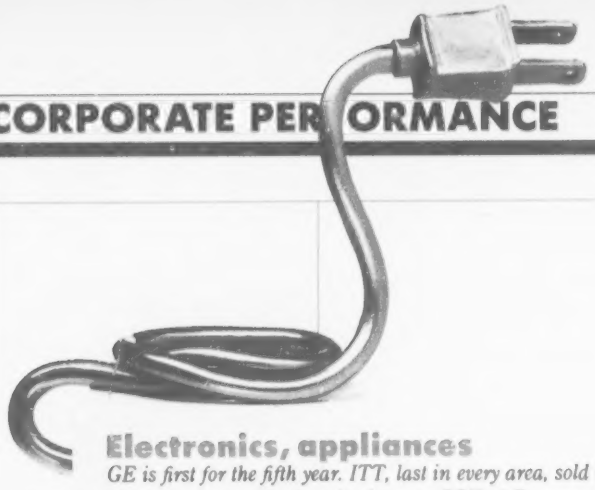


Diversified service

The Tisch takeover could change CBS's scores—especially in management, one of five areas where it's No. 10.

RANK	LAST YEAR	COMPANY	SCORE
1	1	Salomon[2]	7.09
2	2	Super Valu Stores	6.48
3	–	Hospital Corp. of America[1]	6.32
4	4	McKesson	6.27
5	3	Fleming	6.11
6	–	Union Pacific[3]	5.96
7	8	Enron[4]	5.74
8	7	Halliburton	5.71
9	9	Fluor	5.55
10	6	CBS	5.20

[1]Not ranked last year.
[2]Formerly Phibro-Salomon.
[3]Ranked No. 5 last year in the transportation category.
[4]Formerly HNG/InterNorth.



Electronics, appliances

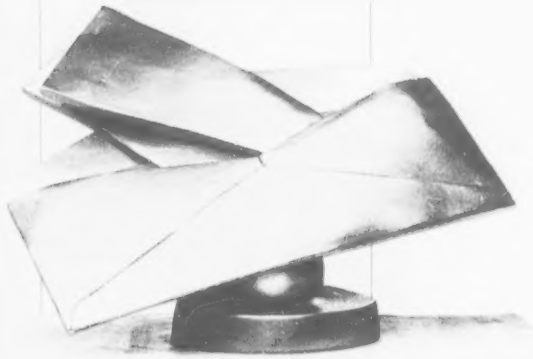
GE is first for the fifth year. ITT, last in every area, sold most of its telecommunications business to CGE of France.

RANK	LAST YEAR	COMPANY	SCORE
1	1	General Electric[1]	7.61
2	2	Emerson Electric	7.08
3	4	Motorola	6.81
4	3	AT&T	6.62
5	–	TRW[2]	6.40
6	5	Raytheon	6.36
7	6	Westinghouse Electric	6.10
8	9	Texas Instruments	5.89
9	8	Litton Industries	5.48
10	10	ITT	5.08

Food

Nobody still doesn't like Sara Lee, No. 1 now that last year's leader, Nabisco, has been merged into RJR.

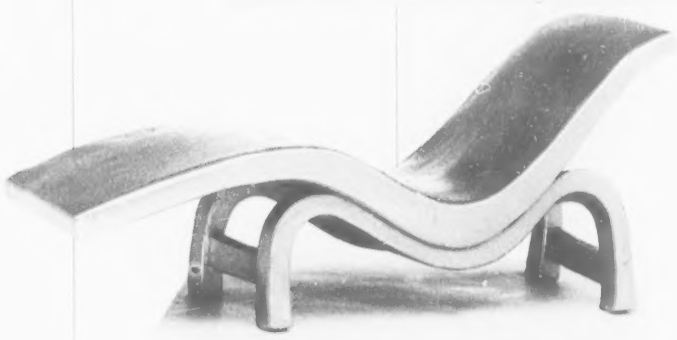
RANK	LAST YEAR	COMPANY	SCORE
1	2	Sara Lee	7.29
2	–	Pillsbury[3]	7.25
3	3	General Mills	7.20
4	6	Ralston Purina	7.04
5	3	Dart & Kraft[4]	6.93
6	–	ConAgra[3]	6.91
7	8	Borden	6.32
8	7	Archer Daniels Midland	6.29
9	9	CPC International	6.06
10	–	IC Industries[3]	6.02



Forest products

Kimberly-Clark leads in half the categories. James River, tops in three, bought last year's industry loser, Crown Zellerbach.

RANK	LAST YEAR	COMPANY	SCORE
1	1	Kimberly-Clark	7.25
2	2	James River Corp. of Virginia	6.73
3	4	Scott Paper	6.35
4	3	Mead	6.00
5	6	Georgia-Pacific	5.89
6	–	Great Northern Nekoosa[3]	5.83
7	7	Boise Cascade	5.73
8	5	Weyerhaeuser	5.66
9	8	Champion International	5.29
10	9	International Paper	4.98

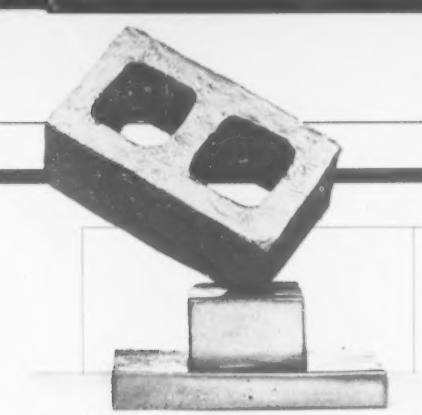


Furniture

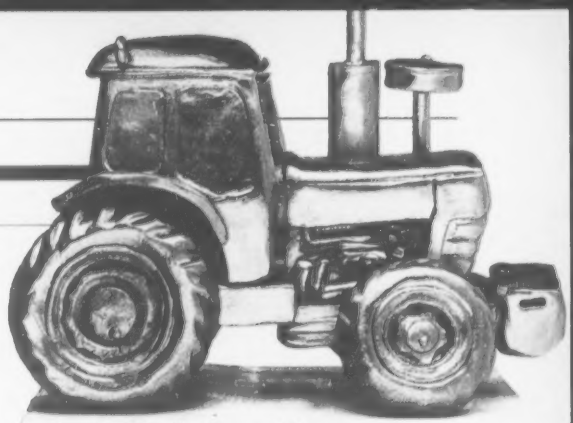
The industry, new to the survey, polished its way to a median score of 7.54, highest of all 33 groups.

RANK	LAST YEAR[5]	COMPANY	SCORE
1	–	Herman Miller	7.84
2	–	Leggett & Platt	7.72
3	–	Hon Industries	7.35
4	–	Mohasco	6.34

[1]Acquired RCA in June 1986.
[2]Ranked No. 5 last year in the motor vehicles and parts category.
[3]Not ranked last year.
[4]Company split into Kraft Inc. and Premark International in October 1986.
[5]This industry was not surveyed last year.



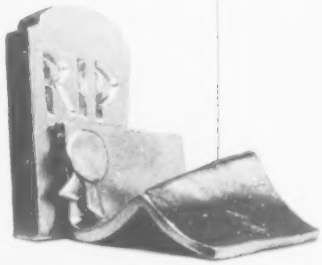
HOW COMPANIES RANK IN 33 INDUSTRIES



Glass, building materials

What's in a name? Libbey-Owens-Ford turned into Trinova and jumped three places up the list.

RANK	LAST YEAR	COMPANY	SCORE
1	1	Corning Glass Works	7.05
2	2	PPG Industries	6.77
3	4	Owens-Illinois	6.36
4	5	USG	6.26
5	8	Trinova[1]	6.00
6	3	Owens-Corning Fiberglas	5.78
7	6	Norton	5.76
8	–	Jim Walter[2]	5.72
9	7	National Gypsum	5.42
10	10	Manville	3.64



Industrial and farm equipment

Caterpillar ranks first in quality of its products. Cummins and Teledyne lead in three areas each.

RANK	LAST YEAR	COMPANY	SCORE
1	1	Cummins Engine	6.98
2	3	Teledyne	6.89
3	–	Black & Decker[2]	6.77
4	6	Caterpillar[3]	6.71
5	2	Deere	6.46
6	–	American Standard[4]	6.35
7	8	Ingersoll-Rand	6.27
8	7	Combustion Engineering	6.13
9	6	Dresser Industries	5.98
10	9	Baker International	5.74

Life insurance

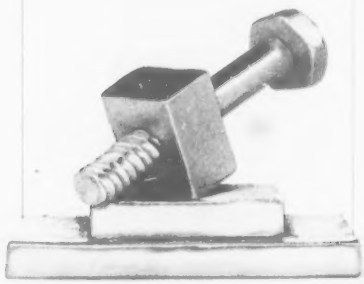
Northwestern Mutual is No. 1 in everything but community and environmental responsibility, where the Rock is at the top.

RANK	LAST YEAR	COMPANY	SCORE
1	1	Northwestern Mutual	7.19
2	2	Prudential	6.57
3	4	Teachers Insurance & Annuity	6.37
4	9	Aetna Life	6.21
5	3	Travelers	6.15
6	5	Metropolitan Life	6.10
7	6	Connecticut General Life	6.07
8	10	New York Life	6.04
9	7	John Hancock Mutual	5.98
10	8	Equitable Life Assurance	5.85

Metals

Alcoa has been No. 1 since 1983. Overall the industry scores lowest in the survey, with a median of 5.22.

RANK	LAST YEAR	COMPANY	SCORE
1	1	Alcoa	6.44
2	2	Reynolds Metals	6.27
3	5	Marmon Group	5.79
4	–	Penn Central[2]	5.52
5	–	Farley/Northwest Industries[2]	5.46
6	4	Inland Steel	4.97
7	7	Kaiser Aluminum & Chemical	4.69
8	8	Armco	4.58
9	9	Bethlehem Steel	3.69
10	10	LTV	3.11



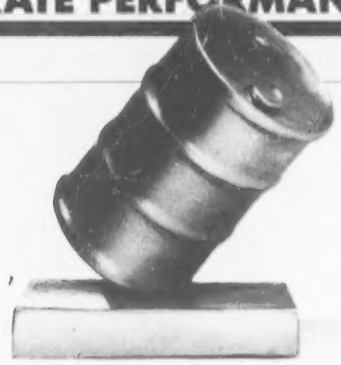
Metal products

It was a close shave, but Gillette fended off invader Revlon and kept first place without a nick in sight.

RANK	LAST YEAR	COMPANY	SCORE
1	1	Gillette	7.00
2	3	Stanley Works	6.95
3	2	Masco	6.71
4	4	Parker Hannifin	6.38
5	6	American Can	6.31
6	–	Emhart[5]	6.28
7	7	Crown Cork & Seal	6.24
8	8	Harsco	5.99
9	9	CBI Industries	5.93
10	–	Triangle Industries[2]	5.73

[1]Formerly Libbey-Owens-Ford
[2]Not ranked last year
[3]Formerly Caterpillar Tractor
[4]Ranked No. 1 last year in the shipbuilding, railroad and transportation equipment category
[5]Ranked No.5 last year in the industrial and farm equipment category

CORPORATE PERFORMANCE



Mining, crude-oil production

In a weak industry, Ohio's Standard Oil finished first in five of the eight categories. Amax was at the bottom in six.

RANK	LAST YEAR	COMPANY	SCORE
1	1	Standard Oil	6.42
2	3	Vulcan Materials	6.14
3	4	Freeport-McMoRan	5.91
4	2	Mitchell Energy & Development	5.85
5	5[1]	International Minerals & Chemical	5.67
6	5[1]	Louisiana Land & Exploration	5.54
7	7	Occidental Petroleum	5.40
8	8	Westmoreland Coal	5.26
9	9	Inspiration Resources	4.77
10	10	Amax	4.41

Motor vehicles and parts

Fueled by the success of its Taurus and Sable models, Ford lapped GM, which fell back three places.

RANK	LAST YEAR	COMPANY	SCORE
1	2	Ford Motor	7.26
2	3	Chrysler	6.94
3	4	Dana	6.65
4	1	General Motors	6.56
5	6	Paccar	6.17
6	7	Borg-Warner	6.07
7	–	Mack Trucks[2]	5.19
8	8	Fruehauf	4.78
9	9	Navistar International[3]	4.72
10	10	American Motors	3.45

Petroleum refining

Despite falling oil prices, Exxon's 9.23 ranking for financial soundness is the highest in the survey.

RANK	LAST YEAR	COMPANY	SCORE
1	–	Shell[4]	7.91
2	1	Exxon	7.80
3	2	Amoco	7.61
4	4	Chevron	6.67
5	3	Atlantic Richfield	6.34
6	6	Mobil	6.28
7	7	Tenneco	5.70
8	8	Texaco	5.06
9	9	Philips Petroleum	5.01
10	10	USX[5]	4.50

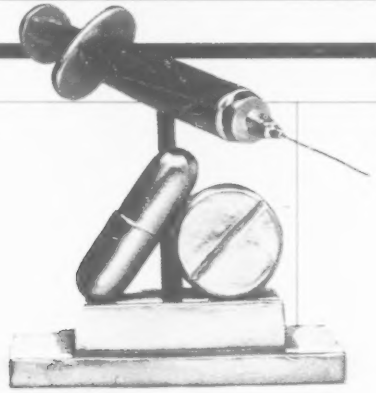
Office equipment, computers

Digital leads in quality of products and services, and Apple in innovativeness. Otherwise, IBM is No. 1.

RANK	LAST YEAR	COMPANY	SCORE
1	1	IBM	7.91
2	3	Digital Equipment	7.75
3	2	Hewlett-Packard	7.58
4	–	Apple Computer[4]	6.83
5	4	NCR	6.18
6	8	Pitney Bowes	5.67
7	5	Wang Laboratories	5.59
8	6	Honeywell	5.47
9	7	Burroughs[5]	5.31
10	10	Control Data	4.34

[1]Tie. Each scored higher than the other last year on four of eight attributes.
[2]Ranked No. 3 last year in the shipbuilding, railroad and transportation equipment category.
[3]Formerly International Harvester.
[4]Not ranked last year.
[5]Merged with Sperry in September 1986, name changed to Unisys Corp. in November 1986.
[6]Formerly U.S. Steel.

HOW COMPANIES RANK IN 33 INDUSTRIES



Pharmaceuticals

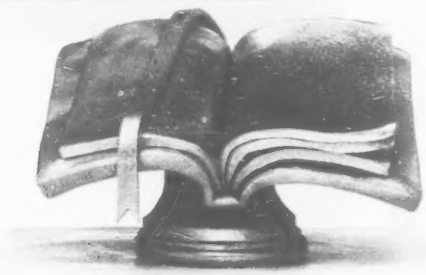
With Merck and Johnson & Johnson in the top ten overall, the industry has one of the best median scores.

RANK	LAST YEAR	COMPANY	SCORE
1	1	Merck	8.38
2	2	Johnson & Johnson	7.86
3	5	Abbott Laboratories	7.47
4	6	Eli Lilly	7.36
5	3	Pfizer	7.35
6	4	Bristol-Myers	7.21
7	7	American Home Products	6.88
8	9	SmithKline Beckman	6.35
9	–	Baxter Travenol[1]	6.07
10	10	Warner-Lambert	6.00

Precision instruments

3M and Kodak tie for best product quality. 3M leads outright in six areas; meanwhile, Kodak is tops in responsibility.

RANK	LAST YEAR	COMPANY	SCORE
1	1	3M	7.69
2	2	Eastman Kodak	6.94
3	3	EG&G	6.70
4	4	Perkin-Elmer	6.64
5	8	Becton Dickinson	6.41
6	6	Xerox	6.40
7	9	Polaroid	6.37
8	5	Tektronix	6.12
9	7	General Signal	5.68
10	10	Lear Siegler	5.64



Publishing, printing

For innovation Gannett is second among 300 companies, but in product quality it's No. 10 in its group.

RANK	LAST YEAR	COMPANY	SCORE
1	1	Dow Jones	7.84
2	2	New York Times	7.80
3	3	Gannett	7.22
4	6	Knight-Ridder[2]	7.08
5	7	Washington Post	7.01
6	5	R.R. Donnelley & Sons	6.97
7	8	Times Mirror	6.88
8	4	Time Inc.	6.74
9	9	McGraw-Hill	6.56
10	10	Tribune	6.55

Retailing

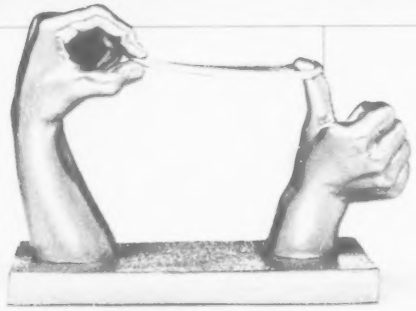
Dayton Hudson, which is selling B. Dalton Bookseller to Barnes & Noble, is tops in all eight components of reputation.

RANK	LAST YEAR	COMPANY	SCORE
1	–	Dayton Hudson[1]	7.25
2	1	Sears Roebuck	6.44
3	3	Kroger	6.35
4	6	J.C. Penney	6.34
5	4	Federated Department Stores	6.21
6	8	K mart	5.98
7	9	Southland	5.96
8	2	American Stores	5.87
9	7	Lucky Stores	5.24

[1]Not ranked last year
[2]Formerly Knight-Ridder Newspapers

CORPORATE PERFORMANCE

HOW COMPANIES RANK IN 33 INDUSTRIES



Rubber and plastic products

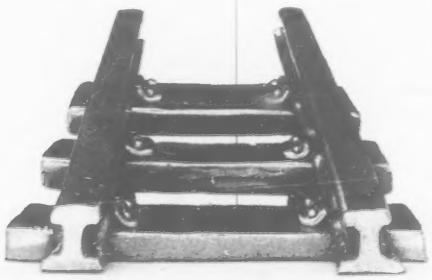
Rubbermaid—which makes mainly plastic products—leads, except for responsibility, where it's No. 2.

RANK	LAST YEAR	COMPANY	SCORE
1	1	Rubbermaid	7.94
2	2	Goodyear Tire & Rubber	7.13
3	6	GenCorp	6.28
4	4	Cooper Tire & Rubber[1]	6.03
5	3	Carlisle[1]	6.03
6	5	Armstrong Rubber	5.72
7	8	Firestone Tire & Rubber	5.45
8	10	B.F. Goodrich	5.44
9	–	Dorsey[2]	5.31
10	7	Dayco	5.23

Savings institutions

In this newly created industry group, Financial Corp. of America ranks at the bottom. It's plagued by problem loans.

RANK	LAST YEAR[3]	COMPANY	SCORE
1	–	Great Western Financial[4]	7.34
2	–	H.F. Ahmanson[5]	7.20
3	–	Home Federal Savings & Loan	6.72
4	–	Golden West Financial	6.54
5	–	Calfed	6.39
6	–	Glenfed[6]	6.08
7	–	First Federal of Michigan	5.44
8	–	Meritor Savings Bank[7]	5.17
9	–	Gibraltar Financial	5.01
10	–	Financial Corp. of America[8]	3.46



Shipbuilding, railroad and transportation equipment

With last year's champ American Standard ranked elsewhere, Fleetwood now rolls into the top spot.

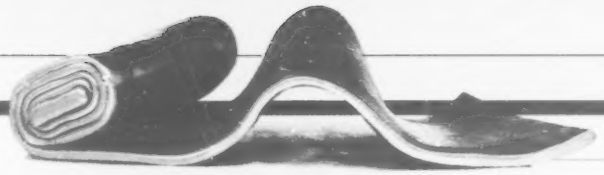
RANK	LAST YEAR	COMPANY	SCORE
1	2	Fleetwood Enterprises	7.22
2	4	Ogden	6.92
3	–	Winnebago Industries[2]	6.79
4	6	Todd Shipyards	6.13

Soaps, cosmetics

P&G is No. 1 in every trait. Revlon, taken over by new Chairman Ronald Perelman, ranks last except for innovativeness.

RANK	LAST YEAR	COMPANY	SCORE
1	1	Procter & Gamble	7.69
2	4	Lever Brothers	6.67
3	3	Clorox	6.56
4	2	International Flavors & Fragrances	6.53
5	6	Colgate-Palmolive	6.35
6	7	Chesebrough-Pond's	6.18
7	8	Avon Products	5.89
8	5	Economics Laboratory	5.86
9	9	Revlon	5.04

[1]Cooper Tire & Rubber scores higher in five of eight attributes.
[2]Not ranked last year.
[3]This industry was not surveyed last year.
[4]Ranked No. 7 last year in the diversified financial category.
[5]Ranked No. 8 last year in the diversified financial category.
[6]Formerly Glendale Federal Savings & Loan Association.
[7]Formerly Philadelphia Savings Fund Society.
[8]Ranked No. 10 last year in the diversified financial category.



Textiles, vinyl flooring

Since the survey was completed, No. 1 Collins & Aikman has agreed to a takeover by Wickes.

RANK	LAST YEAR	COMPANY	SCORE
1	1	Collins & Aikman	7.67
2	3	West Point-Pepperell[1]	7.37
3	2	Armstrong World Industries	7.19
4	4	Springs Industries[2]	7.03
5	5	Shaw Industries	6.86
6	8	Fieldcrest Cannon[3]	6.35
7	9	J.P. Stevens	6.07
8	6	Burlington Industries	6.06
9	–	DWG[4]	5.86
10	10	United Merchants & Mfrs.	4.81

Tobacco

R.J. Reynolds and Nabisco joined forces and pushed Philip Morris into second place.

RANK	LAST YEAR	COMPANY	SCORE
1	2	RJR Nabisco[5]	7.80
2	1	Philip Morris	7.70
3	3	United States Tobacco	6.15
4	4	American Brands	6.14

Toys, sporting goods, musical instruments

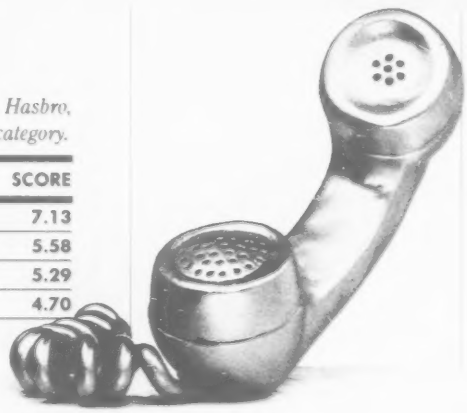
Mattel leads the list of biggest point losers. Hasbro, maker of the G.I. Joe doll, is No. 1 in every category.

RANK	LAST YEAR	COMPANY	SCORE
1	1	Hasbro	7.13
2	2	Mattel	5.58
3	–	Minstar[4]	5.29
4	4	Coleco Industries	4.70

Transportation

UPS delivers a No. 1 ranking in six attributes. AMR is the most innovative, Delta the most responsible.

RANK	LAST YEAR	COMPANY	SCORE
1	1	United Parcel Service	7.33
2	3	AMR (American Airlines)	7.06
3	2	Delta Air Lines	6.91
4	–	Norfolk Southern[4]	6.67
5	6	UAL (United Airlines)	6.44
6	7	CSX	6.20
7	4	Burlington Northern	6.17
8	8	Santa Fe Southern Pacific	5.61
9	–	Trans World Airlines[4]	4.31
10	10	Pan Am	3.73



Utilities

Innovativeness goes to US West, but the pride of Ma Bell's offspring is BellSouth, first in the other seven attributes.

RANK	LAST YEAR	COMPANY	SCORE
1	2	BellSouth	7.37
2	3	Bell Atlantic	7.33
3	1	Ameritech	7.20
4	4	Pacific Telesis Group	7.01
5	7	Nynex	6.93
6	5	US West	6.90
7	6	Southwestern Bell	6.76
8	8	Pacific Gas & Electric	6.62
9	9	Southern	6.42
10	10	GTE	6.28

[1] Acquired Cluett Peabody, which was tied last year at No. 5 with Oxford Industries in the apparel category.
[2] Acquired M. Lowenstein, ranked No. 7 last year in the textiles, vinyl flooring category.
[3] Formerly Fieldcrest Mills.
[4] Not ranked last year.
[5] Acquired Nabisco Brands, ranked No. 1 last year in the food category.

ARE SHAREHOLDERS CHEATED BY LBOs?

Companies taken private by their own managers a couple of years ago are being sold to the public again, at prices two or three times what the stockholders were paid. The company's executives pocket a lot of the difference. Is something fishy going on here? ■ *by Gary Hector*

SECURITY ANALYSTS shuddered when Beatrice Cos. went private early last year. The largest leveraged buyout ever, with a $6.2-billion price tag and $6.1 billion of ulcer-inducing debt, the deal looked like a disaster in the making. Yet in just eight months Beatrice's chief executive, Donald Kelly, has unloaded $6 billion of unwanted businesses and shed nearly $5 billion of debt. Unless the stock market falls apart, Kelly plans to take Beatrice public again in 1987, which could net him more than $400 million personally on an initial investment of $5 million. "This one," says an admiring lender, "will go down in history."

He'll Make $400 Million

Donald Kelly led the $6.2-billion buyout of Beatrice in 1986. He has sold lots of assets, and is now expected to take the company public again.

It is also fueling a debate about whether an LBO like this one is fair to the shareholders. Sure, they collect a fat premium over the going market price when they sell their shares. But do they really get top dollar?

You remember the basic drill on how an LBO works: A group of smart investors, often including the company's management, borrows heaps of money and buys the company. In Beatrice's case, the group included not company insiders but outsiders who *used* to be insiders. Kelly and friends, a legendarily shrewd group of marketers and dealmakers, had run Esmark before it was acquired by Beatrice in 1985. They teamed up with the LBO firm of Kohlberg Kravis & Roberts, which put the deal together and raised the money. Now comes the punch line: A miraculously short time later the company has more than doubled in value, and the value of management's stake has increased 50-fold.

What's going on here? Proponents of management buyouts argue that the discipline imposed by a huge debt and the bliss of being private transform ordinary executives into supermen who work wonders on their organizations. Once a firm goes private, explains Alan Rappaport, a specialist in mergers and acquisitions at Northwestern University's Kellogg School of Management and a consultant, "You are no longer dealing with the same culture. The economic incentives are much more compelling; there is a much higher energy level, a much greater devotion to efficiency and risk-taking."

But the evidence emerging from recent LBOs suggests an alternative explanation. What appears to make buyouts successful is the ability of insiders—or well-informed outsiders like Donald Kelly—to pay rock-bottom prices to take companies private. Unlike the market for a few hundred shares of common stock, the market for control of public corporations seems to be surprisingly inefficient, at least to judge from the astonishingly different amounts the corporate assets command going into and coming out of a buyout.

The critics of LBOs argue that neither the board of directors, the investment bankers helping them out, nor the managers themselves have strong enough incentives to protect shareholders. Indeed, the potential conflicts of interest are so disquieting that a few chief executives are embracing a new financing alternative known as the leveraged cashout. In a cashout the shareholders get not only money up front, but also some stock in the lean-and-mean new company. Some recent cashouts: FMC, Colt Industries, and Holiday Corp.

THE CENTRAL ISSUE in the unfolding debate is the proper relationship between management and shareholders. We all know the theory about how this relationship works: Management acts as an agent for the shareholder, making day-to-day decisions in the shareholders' interests. But when the managers begin cobbling together a tender offer for the company they run, they and the shareholders become opposing parties in a negotiation. The guardian angel in this process is the board of directors, whose duty is to ensure that shareholders don't get roughed up by their management. In practice, critics say, the angel has no wings.

Sure, the critics concede, interest rates have dropped, and yes, the management is better motivated. But can that explain

RESEARCH ASSOCIATE *Margaret A. Elliott*

He Will Collect $3 Billion

Metromedia's John Kluge, 71, shown here with third wife Pat, in her early 40s, has reason to beam. After taking Metromedia private in 1984, he managed to sell off its component businesses for much more than he paid for them. When completed, his dealmaking could net him close to $3 billion.

changes in value like the following: Metromedia Inc., which went private in 1984 for $1.1 billion, is in the midst of a liquidation that has already raised five times that sum. Uniroyal Inc., which went private in April 1985 for $900 million, is in the process of selling off its businesses and seems likely to receive at least $1.4 billion. SFN Inc., a publisher of textbooks taken private for $450 million in early 1985, recently announced plans for a liquidation that will net it close to $1.1 billion. Equally big gains have accrued to owners of smaller companies that have made the round trip, such as Motel 6, Calton Corp., Edgcomb Steel, and Blue Bell Inc.

The money that top executives at these companies make on the deals propels them to the outer limits of the known universe for executive compensation. John Kluge, chief executive of Metromedia, made an estimated *$3 billion* through the liquidation of the company. John Pomerantz, chairman of dressmaker Leslie Fay, which went private in an LBO and then changed hands again in a second LBO, netted $60 million in four years on an initial investment of less than $1 million. Joseph Flannery, chairman of Uniroyal, expects to earn $20 million on an investment of less than $750,000 a year ago. John Purcell, SFN's top executive, made at least $25 million in 18 months on an investment of less than $500,000.

IT'S ENOUGH to raise a few eyebrows. Why, the critics ask, does management have to take a company private before it can work up the moxie to do all those things that improve the corporate prospects so dramatically? "There is something questionable about taking companies private and then, within a relatively short period of time, bringing them public at a substantial increase in value," worries A. A. Sommer, a former member of the SEC. "It would suggest that the public shareholders did not get full value."

LBOs still have staunch defenders. They argue that buyouts, unlike insider trading, occur in the sunshine. Shareholders are told of the deals weeks in advance, vote on the transactions, and collect a big profit by selling out. Buyers must disclose their intentions in proxy statements, the board of directors must bless the deal, and takeover artists may step in and bid on the company, turning the sale into a public auction. "The market for buying and selling companies is pretty efficient," maintains Fred Eckert, a partner at Goldman Sachs. "Nobody does leveraged buyouts over a Saturday night intimate. Any

He Made $60 Million

John Pomerantz did an LBO in 1982 on Leslie Fay, the apparel company his father founded, then brought it public again in 1986. Buyout price: $58 million; sale price on going public: $360 million.

body who has the money can make a bid."

Critics say that in the real world these protections are meaningless. Once a company is "in play," most shareholders take their money and run. The people who then own the stock, the arbitrageurs, operate on thin margins and must turn over their inventory rapidly to realize a profit—in much the same way an efficient supermarket must do.

AND CONSIDER the plight of the board. Directors have a fiduciary responsibility to allow shareholders to vote on any bid that substantially exceeds the current market price, even if the board thinks the bid is well below the firm's potential value. Those savvy investment bankers, supposedly so adept at valuing a company, invariably blow their client's bid with a lengthy document explaining why the bid is a "fair" market price—if not indeed egregiously generous. In one bidding war, for Stokely Van Camp, three different investment advisers provided "fairness" letters to three different prospective buyers at prices ranging from $40 to $75 a share.

When management buys the company, the critics of this movement charge, the bosses know more about the intrinsic value than either the shareholders or the investment bankers. Consider Metromedia. One of the first big leveraged buyouts, Metromedia went private in mid-1984 at the then unprecedented price for an LBO of $1.1 billion. Prospects for its broadcast and cellular radio businesses looked mediocre. The company had been criticized for sloppy accounting practices, which had driven its stock price to a six-year low. John Kluge, Metromedia's chairman and controlling shareholder, decided that the low price left his company vulnerable to raiders, so he took it private, in the process increasing his ownership from around 25% of the company to 93%. In making the deal, he got fairness opinions from Lehman Brothers and Bear Stearns, neither could round up even one competitive bidder. Within months circumstances showed just how risky the deal might prove to be if Kluge was wrong. Metromedia missed a payment on its debt and was forced to refinance. "I really thought this was going to be the one that hit the fan," says a banker who specializes in lending on LBOs.

In retrospect, Kluge knew what he was doing. He decided to dismantle his company and dispose of it piece by piece. He sold seven television stations for $2 billion and found buyers for a radio station, the Harlem Globetrotters, the Ice Capades, and finally for the seemingly doggy cellular radio operation, which fetched $1.1 billion. In all, Kluge has made $5.5 billion by dismantling Metromedia—a fivefold increase in just two years. Everybody admits belatedly that Kluge is some sort of business genius. He sold his TV stations at the peak and nursed along his cellular operations until telephone companies began snapping them up for unheard-of prices. But how much is genius worth? $5 billion? And how much of this prescience did he impart to his shareholders?

Or take a smaller example: the management buyout of Fred Meyer Inc., a Portland, Oregon, retailer. Fred Meyer is a regional version of K mart, a blue-collar retailer with an array of large stores throughout the Pacific Northwest. The chain was built almost single-handedly by Fred Meyer and his family and was closely controlled until 1978, when Meyer died at age 92. Two years later a group of the company's executives, together with Kohlberg Kravis & Roberts, took Fred Meyer private in a transaction that Jerome Kohlberg later described as one of the most complicated he'd ever attempted. The price: $420 million, or $35 a share.

What made Fred Meyer tantalizing was the company's real estate, carried on the books at cost and owned by the company on long-term sweetheart leases from firms jointly owned by the company and the Meyer family. The value of the property was at least $330 million to $340 million more than the

He Made $25 Million

1978's John Purcell took the company private once previous from the founding families. Within a year its assets doubled in value.

price on the Fred Meyer balance sheet.

Potential testimony in a suit brought by the Meyer family about the buyout suggests that Fred Meyer's board never understood the transaction they approved. A special committee of the board, composed of three outside directors (two others were appointed but never attended the meetings), met three times, devoting about six hours to reviewing the proposal. The committee never hired its own advisers. It relied on management's law firm and investment bankers, even though management wound up owning a stake of 10% in the private company. At least two other outside bid engineered an interest in buying Fred Meyer, one of which, a French retailer, had proposed a price $2 a share higher than the KKR bid. Yet the committee never sought other bidders or encouraged management to talk with potential buyers from outside. Even worse, despite a caution by Earle A. Chiles, a board member and Fred Meyer's surgeon, the board never obtained an independent appraisal of the value of the company's real estate.

Minutes of the meeting at which the board accepted the KKR bid show that Martin Siegel, then a Kidder Peabody partner and the buyout group's investment banker, told the board that the offer was low, but "at the low end of the range of fairness." This qualifying observation was never revealed in any material sent to shareholders.

The actual value of Fred Meyer, according to estimates later done for Chiles by James Reinhardt, dean of the school of business at the University of Oregon, was around $70 a share. Even Reinhardt's estimate may have been low. When Fred Meyer went public again this summer, the company's value had increased to more than $900 million, or over $100 a share.

On consider the most recent leveraged buyout of 1979 has, in Cleveland, Ohio's John Patrick, chairman of 1979, took his company private in 1985. Patrick's bid was opposed by three directors, representing the heirs and Protestant families which had founded 1979. They hired an outside investment banker, Smith Barney Harris Upham & Co., and engaged in heated meetings. But the directors should solicit other bids for the company to obtain the highest possible price. The board chose instead to consider Patrick's offer, which stipulated that the company be "sold" not only another Meyer while negotiating with Patrick. The same terms were amended to allow the board to talk with Hallmark Cards, which had expressed an interest in the company but then dropt down to join Patrick's personal group, apparently on the basis a good deal when it was one.

1979's board felt it needed talk to a company like Patrick's group's personnel but by agreeing to consider just one bid, abandoned the chance of an auction. Experts established on about the offer with the help of its investment banking firms, which specified the obligations fully known. But their interest opinions aimed that they never took shopping for other buyers or sought bidders on portions of the company. The oversight is current despite the fact that Hallmark, Time Inc. publishers in Washington, and Gulf & Western each took exploratory an interest in buying 1979 in pieces of it.

A decade after he got control of the company, Patrick proceeded to sell most of the assets he once owned. The largest piece, Rock Productions Publishing, was acquired by Time Inc. for $500 million.

Members of the Scott and Patterson families have written to lawyers for Patrick, saying that they are still so angry that the things they sold might be considered undervalued. One of the other directors who approved the deal publicly owns his shares. "This is a very sore subject with me," says Mary Patrick, an 1979 board member who now is the consultant. Her disagreement with Patrick over Patrick "I thought the way the deal was done was very unfair to them, to be sure. The [1979] the company could have negotiated a better deal for the shareholders."

Miraculous Changes in Market Value

COMPANY	LBO PRICE [illegible]	VALUE WHEN TAKEN PUBLIC OR SOLD	PERCENTAGE INCREASE
BEATRICE	$6.2 billion [illegible]	$12 billion (est.) Assets sold: to-be for $4 billion; Coca-bottling unit for $1 billion; 50% of International Playtex for $1.25 billion; other businesses for $6.75 billion.	93%
KAISER STEEL	$400 million [illegible]	$750 million Sold to 1979 Corp. for $375 million in cash and stock plus assumption of $650 million in long-term debt.	88%
DR PEPPER	$600 million [illegible]	$900 million Assets sold: Canada Dry for $175 million; bottling plants and other businesses sold for $275 million; 7-Up Japan sold for $450 million.	50%
[illegible]	$240 million [illegible]	$360 million Taken public again (1.5x)	50%
[illegible]	$1,000 million [illegible]	$1,500 million Sold to Chrysler Motors (1.5x)	50%
[illegible]	$1.1 billion [illegible]	$1.4 billion (est.) Assets sold: seven TV stations for $1 billion; cellular radio licenses for $1.1 billion; other businesses worth $1.4 billion.	27%
[illegible]	$400 million [illegible]	$600 million (est.) Remaining operations worth $300 million; other assets sold to the real estate syndicate of over $600 million.	50%
[illegible]	$900 million [illegible]	$1.1 billion (est.) Assets sold: book business for $500 million; South Western Publishing for $275 million; TV and radio stations for $325 million.	22%
[illegible]	$900 million [illegible]	$1.4 billion (est.) Assets sold: welding chemicals business for $750 million; other businesses for $500 million; remaining net worth of the unit of the company, $400 million.	56%

Since 1981, 200 public companies have gone private. Of these, some 20 or so have been taken public again or broken up and the assets sold off. The earnings increase is taken for the 20 because being bought and being sold again is always [illegible]. Management should not be complacent.